

Small Business Notes

Minnesota Department of Employment and
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Tax Code Provisions Beneficial to Small Businesses Survive New Tax Law

On January 2nd, 2013, the President signed the “American Taxpayer Relief Act of 2012.” Much of the discussion of potential impacts of earlier versions of the act on small businesses centered around the potential loss of consumer spending and investment in the wake of personal income tax rate increases, and payroll tax increases, scheduled for 2013. As passed the Act retains the current 10 percent, 15 percent, 25 percent, 28 percent, 33 percent, and 35 percent rates while increasing, from 36 percent to 39.6 percent, the tax rate on individuals with income over \$400,000 and joint filers with income over \$450,000. In effect this makes permanent the current tax rates for most Americans. But the Social Security portion of the FICA tax will increase by 2 percentage points to 6.2 percent for employees and 12.4 percent for self-employed individuals up to the base of \$113,700. That increase does have the potential to affect consumer spending but probably has less effect on personal investment decisions.

Title III of the Act, “Business Tax Extenders,” extended and in some cases modified existing business tax incentives. These include:

Research and Development Tax Credit. The “Credit for Increasing Research Activities” of IRC section 41 expired at the end of 2011. The Act extends it to December 31, 2013 and modifies the calculation of the credit to allow companies that acquire a business to partially include pre-acquisition qualified expenses of the acquired business in computation of the credit for the acquiring business.

Section 179 Expensing. IRC section 179 “Election to Expense certain Depreciable Business Assets” allows a business taxpayer to expense costs for tangible property and computer software in the year the property is placed in service rather than over five years or more. The amount of allowable expensing was \$500,000 in 2010 and 2011 with an adjustment downward to \$139,000 in tax year 2012 and to \$25,000 in tax year 2013. The Act extends the \$500,000 limit through 2013 and makes the \$25,000 limit applicable in 2014.

Bonus Depreciation. Under IRC section 168(m) and 168(n) businesses have been able, since 2008, to write off 50 percent of the cost of certain kinds of property (e.g., reuse and recycling equipment, disaster assistance property) in the first year. This provision was set to expire in 2012 but has been extended through 2013.

Exclusion of Gain on Small Business Stock. IRC section 1202 provided for an exclusion of 100 percent of the gain on sale or exchange of qualified small business stock (as defined in the Code) acquired in 2010 or 2011. The Act preserves that exclusion for qualified small business stock acquired in 2010, 2011, 2012 and 2013 and extends the expiration of the exclusion to January 1, 2014.

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Recognition of Built-In Capital Gain on Conversion to S Corporation. IRC section 1374 required that a C corporation converting to an S corporation retain assets for 10 years or pay a 35 percent tax on the built-in capital gain occurring before the conversion. 2009 legislation shortened the holding period to 5 years for assets sold in 2011. The Act extends that five year period through 2013.

Work Opportunity Tax Credit. IRC section 51 provides for a tax credit for employers who hire members of defined targeted groups including veterans, SSI recipients, youth, recipients of long term family assistance. The credit for hiring the disadvantaged expired in 2011 and the credit for hiring veterans expired in 2012. The Act extends both credits through 2013.

New Markets Tax Credit. The IRC section 45D credit for certain qualified investments in a low income community is extended by the Act through 2013 with carryover funds available through 2018.

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